

# Executive Summary

Actuarial and Underwriting Committee Meeting, September 21, 2021

Board of Governors Meeting, September 22, 2021

## Property Inspection Services for Underwriting

### Topic

On July 14<sup>th</sup>, 2021, the Board of Governors approved an Action Item to enter into contracts with the following vendors for Property Inspection Services for Underwriting:

#### Primary Vendors

- C&E Information Services, Inc. (Personal Lines)
- Mueller Services, Inc. (Personal Lines)
- Sutton Inspection Bureau, Inc. of Florida (Personal and Commercial Lines)

Contingent Vendors (to be activated if the Primary Vendors cannot adequately meet Citizens' needs for inspections):

- Inspection Depot, Inc. (Personal and Commercial Lines)
- Insurance Risk Services, Inc. (Personal Lines)

The inspection option presented during the July meeting has been adjusted to account for revised policies-in-force and new submission projections. Automation, new virtual and unit-owner inspections, percent of premium, and FTE impact, have been contemplated in the adjustments, as reflected below:

Previously Proposed Inspection Option - Adjusted									
Year	% of NB	NB Inspection Volume	% of PIF	PIF Inspection Volume	Total Volume	Inspection Vendor Spend	% of Premium	Total FTE Need	Total FTE Cost
2022	6.46%	19,104	5.51%	48,732	67,836	\$3,837,816	0.18%	10.9	\$810,624
2023	8.34%	26,090	6.56%	68,286	94,376	\$4,791,386	0.19%	9.9	\$736,621
2024	11.74%	35,300	8.05%	75,680	110,980	\$5,543,516	0.24%	5.8	\$429,293
2025	12.53%	37,286	11.55%	98,160	135,446	\$6,544,392	0.33%	6.8	\$509,858
<b>4-Year Spend:</b>					<b>408,638</b>	<b>\$20,717,110</b>			<b>\$2,486,396</b>

Along with the above option, Citizens staff agreed to develop an additional option which increases inspection volume over a four-year period (2022-2025). This strategic enhancement to Citizens' inspection plan for 2022-2025, results in an annual increase in inspection volume and associated spend for Personal Lines policies, while maintaining a robust approach for Commercial Lines policies. The projected cost increases are detailed in the recommendation below. An associated Action Item requests additional contract spend for Property Inspection Services for Underwriting to support the implementation of the recommended plan. The originally approved contract amount was \$21,140,000 for the four (4) year base term. Based on current projections in policy growth and implementation of the holistic inspection approach the new contract amount requested is \$43,618,492. Although the inspection types

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may evolve based on market conditions, Citizens' plan is to expand the use of inspections to improve underwriting results and support the exposure reduction strategy.

## Historical

For the last five (5) years, Citizens completed inspections for approximately 1% of its policies on an annual basis with the plan to increase to 2-3% by the end of 2021:

Year	Inspection Volume	Approx. % Of Policies Inspected	Contract Spend	Average Unit Cost
2016 <sup>1</sup>	3,606	0.74%	\$102,730	\$28.49
2017	3,484	0.77%	\$85,614	\$24.57
2018	3,309	0.75%	\$118,249	\$35.74
2019	2,520	0.59%	\$93,780	\$37.21
2020	5,205	1.07%	\$207,610	\$39.89
2021 <sup>2</sup>	20,336	2-3%	\$1,225,085	\$60.24

<sup>1</sup> 2016-2020 based on actual inspection data and PIF counts.

<sup>2</sup> 2021 based on forecast.

At the July Board meeting, Citizens staff shared that from November 1, 2016, through May 31, 2021, there were 21,460 inspections completed for Personal Lines with a total spend of \$783,507. The table below provides updated information through July 31, 2021, showing inspections completed increased to 24,337 with a total spend of \$908,370.

## Volume

Year	General Condition	Mobile Home	Interior/ Exterior	Wind Mitigation	Roof Inspection	Total Volume
2016	2,451	1,155	0	0	0	3,606
2017	2,628	856	0	0	0	3,484
2018	1,849	909	540	0	11	3,309
2019	1,227	852	439	0	2	2,520
2020	3,311	737	995	150	22	5,215
2021 YTD	3312	495	2252	111	33	6,203
Total	14,778	5,004	4,226	261	68	24,337

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## Spend

Year	General Condition	Mobile Home	Interior/ Exterior	Wind Mitigation	Roof Inspection	Total Spend
2016	\$62,095	\$40,636	\$0	\$0	\$0	\$102,731
2017	\$55,464	\$30,151	\$0	\$0	\$0	\$85,615
2018	\$39,593	\$32,277	\$45,873	\$0	\$506	\$118,249
2019	\$25,801	\$30,594	\$37,293	\$0	\$92	\$93,780
2020	\$70,921	\$28,030	\$83,655	\$23,993	\$1,012	\$207,611
2021 YTD	\$70,664	\$19,340	\$191,307	\$17,554	\$1,518	\$300,384
Total	\$324,538	\$181,028	\$358,128	\$41,547	\$3,128	\$908,370

## Market Intelligence

Research conducted on 16 private market carriers showed inspections for underwriting purposes were varied:

- Most carriers require 4-Point Inspections at new business based on the age of older homes. Some carriers require the 4-Point Inspection to reflect systems have been fully updated within the last 15-20 years for eligibility.
- Although some carriers utilize the standard wording, 'all homes are subject to inspection', over half specifically indicated they inspect 100% of the homes at new business; exterior only or both exterior and interior inspections:
  - Exterior for rate accuracy purposes and to confirm condition; and,
  - Full interior and exterior inspections for rating and eligibility purposes.
- Only three carriers mentioned the ordering of inspections at renewal:
  - Inspect as necessary;
  - Inspect homes 30 years old; and,
  - Re-inspect after a loss.
- Two carriers provided inspection cost information as it relates to the % of annual premium spent on their inspection program; 1% and the other at 0.03% of their annual premium.

## Holistic Inspection Plan of Action

Citizens' staff developed a holistic inspection plan for 2022-2025. This plan presents an annual increase in inspection count and associated spend for Personal Lines policies, while maintaining a robust approach for Commercial Lines policies. The details of the plan are shared in the table below.

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Recommended Inspection Option									
Year	% of NB	NB Inspection Volume	% of PIF	PIF Inspection Volume	Total Volume	Inspection Vendor Spend	% of Premium	Total FTE Need	Total FTE Cost
2022	13.30%	39,330	6.89%	60,915	100,245	\$5,682,901	0.26%	16.0	\$1,195,302
2023	20.58%	64,399	10.50%	109,258	173,657	\$8,971,637	0.36%	18.1	\$1,351,775
2024	41.07%	123,551	12.88%	121,088	244,639	\$11,891,457	0.52%	12.4	\$924,210
2025	62.47%	185,855	20.21%	171,780	357,634	\$17,072,496	0.87%	18.0	\$1,321,522
<b>4-Year Spend:</b>					<b>876,176</b>	<b>\$43,618,492</b>			<b>\$4,792,809</b>

*\*This table illustrates year-by-year inspection volume, total inspection-vendor spend, percent of premium, and FTE need/cost.*

This is an estimate of what we plan to accomplish through 2025. As inspection data is obtained, we will test and measure the impact to better understand targeted benefits. As we fine tune the inspection focus actual results and any significant adjustments will be presented at future board meetings.

The recommended inspection option:

- Is in line with current market intelligence, which has a greater focus on new business inspections. Also, the percent of annual premium spent on underwriting inspections falls within current market practice.
- Incorporates automation, allowing a percentage of inspections with low to no risk to bypass underwriting review. In 2024, we anticipate the automation factor to be increased to 75% resulting in a decrease in FTE need for that year. The automation factor remains at 75% for 2025, however, due to an increase in overall inspection volume, total FTE need increases.
- Includes a new, lower cost, highly scalable Virtual Inspection type.
- Establishes condo-unit inspections (HO-6 and DP-3-C).

## Inspection Vendor Support

Given the current market environment, Citizens' desire to increase inspections require a pool of inspection vendors that can provide high quantity and quality inspection services in a timely manner. We have confidence in the contracted inspection vendors' capabilities to perform the recommendation offered above.

Most inspections completed in the past were General Condition and Mobile Home Tie-Down inspections (exterior only) that are less costly. Citizens desires to increase its use of other types of inspections going forward to provide better insight on a property's interior and exterior, including the condition of the roof, plumbing, electrical, and HVAC (heating, ventilation, and air conditioning) systems. Inspections requiring access to the interior and exterior have a higher price point than exterior-only inspections, and this is reflected in the expected price range for 2022 through 2025 in the table below:

Inspection Type	Expected Price Range
General Condition	\$20 - \$35
Interior/Exterior	\$85 - \$95
Mobile Home Tie-Down	\$40 - \$45
All Others (est. < 1%)	--

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## Commercial Lines Inspections

Commercial Lines Underwriting already orders inspections on 100% of new business and the plan is to continue through year 2025. In addition, inspections are ordered by in-office underwriters to address identified underwriting concerns on existing business.

Policies are issued based on the information provided by the agent and approved by underwriting via PolicyCenter. When the policy is issued, an inspection is performed by a Commercial Field Underwriter. The inspection is used to confirm various underwriting characteristics such as construction, occupancy, replacement cost, eligibility, condition, and protection.

Certain municipalities require 40-year (and every 10-years, subsequently) re-certification reports to determine structural stability or condition of buildings. We plan to leverage those known requirements instead of Citizens initiating engineering reports for those properties. Currently, we are requesting these reports on all new business that meets the required thresholds in both Broward and Miami-Dade Counties.

We have filed rules to specifically address the structural inspection requirements for Miami-Dade and Broward Counties and any other structural inspection requirements that are implemented by any other jurisdiction. This rule shall allow us the ability to require 40-year recertification reports when prudent, at the insureds' expense.

Changing market conditions may result in an increased number of commercial submissions over the coming months and years. To maintain Citizens ability to inspect new and existing business, we plan to increase the use of third-party vendors to perform future inspections, as further described below:

Year	General Condition-4PT Inspection			Replacement Cost Valuation			Total Volume & Spend	
	Volume	Avg Unit Cost	Spend	Volume	Avg Unit Cost	Spend	Volume	Spend
2022	300	\$140	\$42,000	300	\$180.00	\$54,000	600	\$96,000
2023	300	\$140	\$42,000	300	\$180.00	\$54,000	600	\$96,000
2024	300	\$143	\$42,900	300	\$184.00	\$55,200	600	\$98,100
2025	300	\$143	\$42,900	300	\$184.00	\$55,200	600	\$98,100
<b>Total Estimated Commercial Lines Contract Spend</b>								<b>\$388,200</b>

## Future State

Citizens will begin taking the necessary steps to significantly expand the use of inspections by leveraging existing and emerging technologies to gain efficiencies to positively impact underwriting results. This holistic inspection approach involves:

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- Accelerating the use of predictive modeling for both new business inspections and renewal inspections.
- Exploring virtual inspection options leveraging aerial imagery and 3<sup>rd</sup> party data such as tax records, building permit data, and other resources.
- Using technology to reduce or eliminate current manual workflow steps related to inspections.

## Summary

The 4-year plan to increase the volume of inspections is going to achieve these critical business results:

- Reduce Loss Frequency – Property inspections, whether conducted during the 90-day discovery period for new business or prior to renewal decisions being made, allow Citizens to guard against adverse selection. We expect to see a 10–20% improvement in the overall impact on loss frequency for inspected policies.
- Improve Premium Accuracy – Property inspections provide observed validation of rating characteristics, directly impacting premium accuracy. In addition to identifying undervaluation concerns, this is going to assist in improving premium accuracy on policies Citizens acquires via Office of Insurance Regulation (OIR) Consent Orders.
- Reduce Exposure via Assumptions by Private Market Insurers – A current inspection is one of the key items private insurers have told us they value when considering which Citizens risks to assume. The more risks we inspect, to validate the exposure they truly represent, the better positioned we are to increase the amount of risk removed from Citizens. We expect an increased assumption ratio of 10-20% for risks inspected. This could equate to an additional \$358M-\$716M in Total Insured Value (TIV) assumed annually.

## Recommendation

Staff proposes that the Actuarial and Underwriting Committee review, and if approved, recommend the Board of Governors:

- a) Approve an increase to the contract spend authority for the Property Inspection Services for Underwriting contracts and vendors listed in the Contract ID section above to \$43,618,492 during the initial four (4) year base term of the contract; and,
- b) Authorize staff to take any appropriate or necessary action consistent with this Action Item.

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## DEFINITIONS

% of Premium: The percentage of annual premium spent on underwriting inspections.

4-Point Inspection: A physical inspection that identifies and describes all electrical, mechanical (HVAC), roofing, and plumbing systems. This includes an evaluation of the condition, identification of any hazards present, and verification of repairs or upgrades required or completed. The inspection documents the current age or year updated of each primary system component and should include photographs. Inspection reports document the remaining life of the predominant roof and secondary roof and any need for repair or replacement of the roof as well as need for repair or replacement of all other systems.

Assumption: An authorized insurance company in the private market removes the risk from Citizens and issues a replacement policy. A private insurance company must be approved by the Office of Insurance Regulation before it can assume Citizens' policies. Any active Citizens policy may be selected for assumption.

Automation: As it relates to inspections, involves categorizing the types of inspection result codes into 4 levels: no concern, low, medium, high; and determining which inspections need to be reviewed by an underwriter versus those that go straight to the underwriting file.

General Condition Inspection: A physical inspection of the building(s) to document the condition of the property and appurtenant structures and identify any property and/or liability hazards or maintenance issues present.

Loss Frequency: The probable frequency, within a given timeframe, that a threat action will result in loss.

Mobile Home Inspection: Physical inspection that identifies the general condition of the mobile/manufactured home, including any hazards or maintenance issues observed. In addition, it identifies the method and materials used to secure it to the ground by the use of anchors and tie-downs so as to resist wind overturning and sliding, in accordance with Florida Statutes.

Predictive Modeling: Predictive modeling at Citizens looks at outcomes from historical data to determine statistically significant policy/claim characteristics that have demonstrated higher propensity for a particular outcome to occur (i.e. data inaccuracies or likelihood for a claim). This information is used to help improve business processes to increase efficiencies and reduce costs without sacrificing service to stakeholders.

Replacement Cost Valuation: A physical inspection and measurement of the subject building(s) and/or appurtenant structures with information entered into a replacement cost estimation tool. This inspection includes supporting photos.

Roof Inspection: A physical inspection that documents the condition of the roof. The inspection includes photographs, identifies roof covering material, roof age in years, remaining useful life in years, date of

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last roofing permit, date and detail of last update, overall condition, visible signs of damage or deterioration, and visible signs of leaks.

Virtual Inspection: Includes overhead and oblique views of the property captured through aerial imagery. These images could include measuring tools. The inspection could include data obtained from property appraisal records, permit data, realtor data, etc.

Wind Mitigation Inspection: A physical property inspection along with the completion of a Florida Uniform Mitigation Verification Inspection Form (OIR-B1-1802), which describes the existence of all allowable wind loss mitigation features. This inspection includes supporting photos.



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**ACTION ITEM**

**New Contract**

**Contract Amendment**

**Other** \_\_\_\_\_

**CONSENT ITEM**

**Contract Amendment**

**Existing Contract Extension**

**Existing Contract Additional Spend**

**Previous Board Approval** \_\_\_\_\_

**Other** \_\_\_\_\_

**Action Items:** Items requiring detailed explanation to the Board. When a requested action item is a day-to-day operational item or unanimously passed through committee it may be moved forward to the board on the Consent Index.

**Move forward as Consent:** This Action item is a day-to-day operational item, unanimously passed through committee or qualifies to be moved forward on the Consent Index.

**Consent Items:** Items not requiring detailed explanation to the Board of Governors. Consent items are contract extensions, amendments or additional spending authorities for items previously approved by the Board.

**Purpose/Scope**

On July 14th, 2021, the Board of Governors approved an Action Item to enter contracts with three primary vendors and two contingent vendors for Property Inspection Services for Underwriting. As further described in the associated Executive Summary, this Action Item requests additional spend authority to accommodate strategic enhancements which provide a holistic inspection approach to Citizens’ inspection plan for 2022-2025. The revised “Holistic Inspection Plan” presents an annual increase in inspection volume and associated spend for Personal Lines policies, while maintaining a robust approach for Commercial Lines policies.

Property inspections are used in the Personal Lines and Commercial Lines underwriting process to make more informed risk-based decisions. Inspections are used for new business applications, endorsement requests, and policy renewals. Citizens’ plan will expand the use of inspections to improve our underwriting results and support our exposure reduction strategy. Currently, the primary inspection types include:

- General Condition
- Interior/Exterior
- Mobile Home
- Roof Inspection
- Proof of Repair
- Wind Mitigation
- High Value Property
- Replacement Cost Valuation, and,
- Virtual Inspections.

**Contract ID**

**Property Inspection Services for Underwriting**

Contract numbers: 21-20-0022-01 through 21-20-0022-05

	<p><u>Primary Vendors:</u></p> <ul style="list-style-type: none"> <li>• C&amp;E Information Services, Inc. (Personal Lines)</li> <li>• Mueller Services, Inc. (Personal Lines)</li> <li>• Sutton Inspection Bureau, Inc. of Florida (Personal and Commercial Lines)</li> </ul> <p><u>Contingent Vendors</u> to be activated if the Primary Vendors cannot adequately meet Citizens’ needs for inspections:</p> <ul style="list-style-type: none"> <li>• Inspection Depot, Inc. (Personal and Commercial Lines)</li> <li>• Insurance Risk Services, Inc. (Personal Lines)</li> </ul>
<p><b>Budgeted Item</b></p>	<p><input checked="" type="checkbox"/> Yes</p> <p><input type="checkbox"/> No</p> <p>Funding for the anticipated inspections in the amount of \$5,682,901 will be included in the upcoming 2022 budget request. Funding for the subsequent contract years of 2023 – 2025 will be budgeted in the appropriate budget year.</p>
<p><b>Procurement Method</b></p>	<p>Citizens issued Invitation to Negotiate No. 20-0022 for Property Inspection Services for Underwriting on October 2, 2020. Seven (7) responses were received and evaluated. The Evaluation Team advanced five (5) vendors to negotiations and following multiple negotiation sessions, on March 24, 2021, the Negotiation Team recommended an award to the five (5) primary and contingent vendors listed in the Contract ID section above.</p>
<p><b>Contract Amount</b></p>	<p>The originally approved contract amount was \$21,140,000 for the four (4) year base term. Based on current projections in policy growth and implementation of the holistic inspection approach the new contract amount requested is \$43,618,492.</p>
<p><b>Contract Terms</b></p>	<p>The contracts have a four (4) year base term and two (2) optional two (2) year renewals. At this time, Staff is not seeking approval to exercise the optional renewal options.</p>
<p><b>Committee Recommendation</b></p>	<p>Staff proposes that the Actuarial and Underwriting Committee review, and if approved, recommend the Board of Governors:</p> <ol style="list-style-type: none"> <li>a) Approve an increase to the contract spend authority for the Property Inspection Services for Underwriting contracts and vendors listed in the Contract ID section above to not exceed \$43,618,492 during the initial four (4) year base term of the contract; and,</li> <li>b) Authorize staff to take any appropriate or necessary action consistent with this Action Item.</li> </ol>

<b>Board Recommendation from Committee</b>	If approved at its September 21, 2021 meeting, the Actuarial and Underwriting Committee recommends that the Board of Governors: <ul style="list-style-type: none"><li>a) Approve an increase to the contract spend authority for the Property Inspection Services for Underwriting contracts and vendors listed in the Contract ID section above to not exceed \$43,618,492 during the initial four (4) year base term of the contract; and,</li><li>b) Authorize staff to take any appropriate or necessary action consistent with this Action Item.</li></ul>
<b>Contacts</b>	Kelly Booten, Chief Operating Officer Scott Crozier, Vice President – Underwriting and Product Development Stephen Guth, Vice President – Enterprise Services